



CITY OF MONTPELIER, VERMONT

- THE SMALLEST CAPITAL CITY IN THE UNITED STATES -

Mayor Mary S. Hooper

City Council:

Tom Golonka
Andy Hooper
Sarah Jarvis
Nancy Sherman
Angela Timpone
Alan Weiss

William Fraser,
City Manager
wfraser@montpelier-vt.org

Beverlee Pembroke Hill
Assistant City Manager
bhill@montpelier-vt.org

MEMORANDUM

To: Mayor Hooper & City Council Members
From: William Fraser, City Manager
Re: District Heat Project
Date: April 12, 2011

Since we will be warning a special election for either May 17th or 24th, the logical question arises as to whether we will combine the petitioned tax exemption item with a potential district heat bond vote. I've already provided you with an outline of potential dates and deadlines for those special elections. I recommend that the Council support this project and plan for a bond vote on June 14th.

As you choose whether to include District Heat on the earlier meeting, I wanted to update you on this project.

What we know:

- The Federal Government awarded the city an \$8 million grant for a district energy project done in partnership with the State. The grant also included start up money for a Property Assessed Clean Energy (PACE) district.
- The Governor proposed \$7 million in State Capital funds for this project.
- \$7 million was included in the Capital Bill and Budget which has passed the House of Representatives.
- The Montpelier School Board voted to support the project and understands that participation is a 20 year commitment.
- The total project will cost between \$18.2 million and \$20 million depending on final costs of the plant and distribution route. Assuming approval of the State capital funds and a city bond of \$2 million, \$18.2 million in funding is accounted for.

- The city has retained a firm to identify the optimal distribution route, update cost estimates for the route, work with the state on the final overall costs and meet with private property owners. That work is happening now.
- The city has applied for up to \$1.75 million in grants and/or 0% interest loans from the Clean Energy Development Fund.
- The three city buildings (City Hall, Fire Station and Police Station) and two school buildings (Union Elementary School and Montpelier High School) use 100,000 gallons of oil each year. Every dollar that oil increases in price costs the community \$100,000. As illustration, our original financial models for this project were developed using \$2.45 per gallon for #2 heating oil in 2010 and \$2.69 in 2011. The city is currently paying \$3.70 – a difference of \$100,000 per year.
- The State of Vermont will own and operate the upgraded and expanded central heating plant. They will provide bulk heat (hot water) to the city's distribution system which will provide heat to city & school buildings as well as private customers. The city will purchase the bulk heat, supply it to city buildings and resell it to non-city buildings.

What we don't know:

- Whether the Senate will approve the capital funding. We will know this by the end of the session, currently projected for the first week in May.
- Whether CEDF will approve the city's request and what the mix of grant and loan might be. We will know this on April 27th.
- Whether the city council will put forward a bond vote and whether the voters will approve it. The final number for a bond vote will depend somewhat on the package from CEDF, any amount of 0% interest loan must be included in any financing authorization. If not included in the tax exemption election, the decision to go to bond vote should be made by the May 11th council meeting for a vote on June 14th.
- The precise final route of the distribution system and final cost projections. These are being generated and should be clearer by early May.
- All details of the agreement for heat purchase with the state. This is being negotiated now, we have a general outline of agreed upon concepts.
- The actual price of heat for public and private customers. We are projecting that the district heat price will come in around \$29 per MMBTU which is equivalent to \$2.80 per gallon of fuel oil. This will become firmer as we complete negotiations with the state.
- Without a firm price and route details, we do not have firm commitments from private customers. Although the project has been set up to work financially without them, they are not only important to success but, in fact, one of the main reasons to do the project in the first place. We have expressions of interest which will firm up when we can present a price, a route, a cost of conversion and the PACE program to finance the conversion.

Why are we pursuing this project?

- It reduces toxic emissions in downtown Montpelier by as much as 11 tons per year. It is consistent with state and local policy to move to cleaner, renewable energy sources.
- It replaces oil as a prime fuel source with a locally/regionally produced fuel source keeping that economic activity in the northeast.
- It provides stabilization for fuel costs to the state government, city government and school department allowing tax dollars to be redirected toward services or infrastructure rather than oil. As mentioned earlier, \$1 in fuel prices = \$100,000 per year for these buildings.
- It presents an economic development opportunity in downtown Montpelier by providing a cleaner and potentially cheaper source of heat for building owners.
- It mirrors the decision many local homeowners have already made on their own, we are essentially converting downtown to a wood stove.
- The local costs (bond payments, bulk heat costs, operating costs) are being paid out of monies already being used to heat and maintain heat systems in local public buildings. This is Vermont – we will always heat the schools, city hall, fire station and police station. This is not money that can be used for other public purposes. We are spending current fuel system money on a fuel system.
- The State of Vermont converted their district heat system to wood (primarily) in the early 80's following the first "energy crisis". After 30+ years of operating this system, the State is seeking to upgrade and expand it, not abandon it. They have no interest in returning to an oil based heating system and do not second guess their conversion decision at all.
- This is proven technology. As noted above, a district heat system has existed in Montpelier since the 40's and has been wood fired since the 80's. These systems exist and run successfully in both the US and in Europe. This is bolstered by the fact that our partner, the State of Vermont, is a long term presence in our city and will not be closing, off shoring or relocating.
- The city received the largest (\$8 million) energy grant in the nation to support this project. The State and City combined will be able to develop an \$18-\$20 million capital improvement - which cuts annual costs, is environmentally friendly and supports the local economy - for \$9 +/- million in State and City capital funds.

What are the concerns?

- The biggest fear is the fear of change and the unknown. Like the current health care system, oil based heat for our major buildings is all we know. While we complain about costs or problems, we are reluctant to abandon a system for fear that a new system will leave us lacking.

- Although the costs are paid with existing fuel dollars, the city will have to issue a bond to finance the project. The city has a high debt load now and concern exists that if users leave the system, the city will be left holding the indebtedness. This is mitigated somewhat because financial projections don't include private interests.
- The city is speculating on a new heat system. What if something better comes along? This is a fair concern. However staying with our present heating system is also speculating on oil prices and that future alternatives will be as financially feasible as this proposal now which comes with an \$8 million federal subsidy.
- Construction of this project will cause disruption to the downtown area. Like any major project it will be managed but there is no getting around the fact that this requires laying pipes underground throughout downtown. Obviously the idea is that the end heat product is worth it. Another benefit is that when closing streets and sidewalks back up, they can be repaved and rebuilt which is needed in many cases. We could potentially target city capital budget funds for downtown improvements to be done in conjunction with this work.
- The City is assuming a new operational responsibility. In other district heat locations, maintenance work is minimal. The state will be running the heat plant, we will be a customer. There will be administrative work for billing, meter reading etc. but there will also be revenue produced from those activities.
- We don't have all the information. This is a very complex project involving the federal, state and city governments. We are gaining more knowledge, developing more information and accomplishing more project related tasks each week. While some important details are still emerging, the basic structure, costs and contributions are pretty well established. And we have another month to fine tune our information even more.

Conclusion: I have maintained a critical distance and withheld my endorsement throughout the project development in order to objectively analyze the pros and cons and to provide you my best professional advice about how to proceed. I have asked the same questions that all of you have.

I see this as a once in a generation chance to make a bold move which has positive environmental and economic impact. It's easy to support or oppose this project for emotional, philosophical or ideological reasons. I have tried to remove all of those from my work on this and weigh the costs and benefits. On balance this is a solid project which has been in the works for at least 16 years if not more. Given the federal dollars available, the time is now. I made a commitment to you that the project would stay within our current payment stream and it does so. I also made a commitment to you that project finances would not rely on unidentified private customers and it does not. I think that 10 years from now, no one will be wishing that the community had remained on an oil based heat system.

The final decision and details can be addressed at the May 11th meeting when we know the results of the CEDF process and the state budget.